WITNESS STATEMENT OF
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HOUSE COMMITTEE ON SMALL BUSINESS

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Chairwoman Velazquez, Congressman Chabot, and distinguished members of the Committee, thank you for the opportunity to appear today and outline the U.S. textile industry's perspective on the pending free trade agreements (FTAs) with Peru, Colombia, Panama and Korea.

My name is Cass Johnson, and I am President of the National Council of Textile Organizations (NCTO). NCTO is a not-for-profit trade association established to represent the entire spectrum of the United States textile sector, from fibers to yarns to fabrics to finished products, as well as suppliers in the textile machinery, chemical and other such sectors which have a stake in the prosperity and survival of the U.S. textile sector. NCTO is headquartered in Washington, D.C., and also maintains an office in Gastonia, North Carolina.

In this testimony, I would like to touch on a number of issues, including the make-up of the U.S. textile industry, the impact that free trade agreements with Peru, Colombia, Panama and Korea will have on U.S. textile manufacturers and the need for a trade policy agenda that delivers benefits to manufacturers that produce in the United States and employ millions of workers here at home.

About this last point, I would like to make one initial observation. The 2006 elections demonstrated clearly that most Americans believe that trade policy has been headed in the wrong direction and needs to reverse course. As we debate what changes might be made, I implore you to keep your attention focused on rebalancing the playing field to make sure that American jobs stay here. U.S. workers are the most productive, creative and highest-skilled workers in the world, but our trade policy has tilted the playing field against them. Our goal should be to rebalance the field so that they can keep their jobs.

Given that Congress is considering the reauthorization of the Trade Adjustment Assistance (TAA) program this week, I would like to emphasize that after visiting many textile plants across this country and talking with textile employees about their hopes for the future, I can say with confidence that workers in the U.S. textile industry would prefer Congress advocate policies that help preserve their jobs rather than compensate them for lower paying jobs they must take once their jobs are gone. While there is certainly a need for trade adjustment assistance in today's environment, Congress continues to hold-up the TAA program as the cure for all of our trade woes while refusing to address the underlying problem, which is a poorly crafted trade policy framework that is eroding our middle class, deepening the divide between the haves and have nots and a hollowing out of the U.S. manufacturing base.

Far more than implementation of more FTAs, U.S. workers need a trade policy that concentrates on retaining jobs in this country and exacts penalties on those countries that break the rules. The biggest example is China. As NCTO recently testified before the International Trade Commission, China

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gives its textile and apparel sector 73 different subsidies. On top of that, China manipulates its currency, which gives China an additional estimated 20-40 price advantage against U.S. producers. The U.S. Economic and Security Commission determined that China's bad practices have cost the U.S. more than 1.5 million manufacturing jobs over the last ten years. Through its institutionalized effort to dominate world trade in manufactured goods, China has become the most predatory, protectionist power the modern world has ever seen. And yet China continues to get a virtual free pass, both from the Administration and the U.S. Congress. This is unconscionable and is one of the primary reasons that U.S. trade policy is consistently given a failing grade by the American people. While we are supportive of a number of upcoming free trade agreements, if we were to ask Congress to do one thing on trade for the U.S. manufacturing sector, it would not be to pass another free trade agreement but instead to pass a bill that holds China accountable for its currency manipulation and subsidy schemes[1]. This one step would yield more benefits to U.S. manufacturing than a dozen well crafted Free Trade Agreements.

While the focus of this hearing is not trade policy in general, we have appended nine action items that we feel Congress should consider implementing in order to restore faith in U.S. trade policy and to rebalance the trade equation with countries such as China.

U.S. Textile Industry Background

First, I would like to debunk some commonly held beliefs about the U.S. textile industry. I have often heard members of Congress and numerous retailers and importers refer to our industry as not prepared to meet the challenges of manufacturing in the 21st Century. In fact, these comments are not true.

The U.S. textile sector continues to be one of the largest manufacturing employers in the United States. The overall textile sector employed 900,000 workers in 2006.

Our industry is the third largest exporter of textile products in the world exporting more than $16 billion in 2005. These exports went to more than 50 countries, with 20 countries buying more than $100 million a year.

The U.S. textile sector is a very important component of our national defense and supplies more than 8,000 different textile products a year to the U.S. military. The industry spends enormous resources on research and development each year to ensure that our military continues to be the most well-equipped and technologically-advanced military in the world.

From 1994 to 2004, the U.S. textile industry invested more than $33 billion in new plants and equipment and has increased productivity by 49 percent over the last ten years. This investment has secured our second place ranking among all industrial sectors in productivity increases over the past ten years.

As you can see, the U.S. textile industry is an innovative, productive industry that can compete against anyone in the world.

Unfortunately, our industry, as well as much of manufacturing, has been hamstrung by decades of trade policy initiatives that have created a disincentive to invest in this country and to employ workers

[1] Specifically, NCTO strongly supports HR 2942 because it is the only bill before Congress that gives companies in the United States the ability to fight back on currency manipulation. This is principally because it allows U.S. firms to bring countervailing duty cases against China for currency manipulation.

in this country. The free trade agreements I will discuss today are a mixed bag when it comes to the policy goals achieved under the frameworks of these agreements and the impact this will have on the U.S. textile industry.

U.S. Textile Industry FTA Guidelines and Objectives

Generally speaking, the textile industry as a whole has consistently urged that the benefits of free trade agreements must accrue only to those countries who are actual parties to the agreement. In a simple phrase, there must be no third party "free riders" who realize benefits without making any sacrifices of their own. As such, our industry has identified four key policy tenets that must be effectively addressed as part of any free trade agreement in order for these agreements to benefit U.S. textile manufacturers. These include a strong yarn-forward rule of origin, fair and balanced short supply procedures, tariff phase-out schedules that reflect fair market principles, and effective customs enforcement rules and regulations are the primary objectives for the domestic industry in all FTA negotiations.

Rules of Origin:

Specifically, the yarn-forward rule of origin should be uniform and simple for all FTAs. The rule of origin should not provide for exceptions including tariff preference levels (TPLs) and/or cumulation. TPLs and cumulation are exceptions to the rule of origin which allow third-party free-riders, such as China, India and others, who are not party to the agreement and therefore have made no sacrifices or concessions under the agreement, to reap the benefits of the FTA at the expense of U.S. textile manufacturers and textile and apparel manufacturers in the FTA partner country.

This occurs because when TPLs and/or cumulation are included in a FTA, third-party countries, like China and India, can sell yarns and fabrics to the FTA partner country for assembly into apparel and this apparel still enters the U.S. duty-free under the FTA. Under such a procedure, the U.S. textile industry is effectively cut-out of this market.

As I mentioned earlier, the U.S. textile industry is dependent upon exports for its very survival. When important export opportunities are destroyed because of loopholes that are rigged against us, then the industry will strongly oppose those FTAs.

Short Supply:

In addition to rule of origin, ensuring an effective short supply process is included in the agreement is also paramount. NCTO, with very few exceptions, does not object to the inclusion of short supply procedures in an FTA nor the inclusion of items already approved under the short supply provisions of NAFTA, AGOA, ATPDEA, or CBTPA. I cannot emphasize enough, however, that NCTO can only continue to support these mechanisms if they are structured in a way that reflects the true nature of textile production in the United States. Unnecessary loopholes and broad rules that allow for significant third-country inputs through manipulation of the short-supply process will undermine the spirit of FTA agreements as well as threaten the viability of the U.S. textile industry and other trade preference programs. As such, NCTO has consistently urged the development of meaningful rules on short supply, cut-and-sew and knit-to-shape that reflect a realistic assessment of the commercial availability of textile products in the U.S.

In furtherance of this objective, NCTO, along with three other textile trade associations, recently submitted a letter to the Committee for the Implementation Agreement (CITA) outlining our concerns regarding a "new" short-supply process that was initiated under the CAFTA agreement.

During the CAFTA negotiations, offshore apparel and importing interests sought a major revamping of the "NAFTA" short supply model. The revamped model included in CAFTA clearly benefits importing, retailing and offshore interests by substantially expediting the process and incorporating new concepts that facilitate approvals such as restricted-quantity short supply designations. Compared to the NAFTA-type provisions in previous free trade agreements, the CAFTA commercial availability process also significantly weakens the standards by which petitions are evaluated, making it much easier for products to be granted short supply designations. As a result, the CAFTA process represents a major concession on the part of the domestic textile industry and one which was agreed to in good faith in an effort to maximize benefits under the CAFTA.

During the CAFTA negotiations, all parties expressed concerns about efforts by unscrupulous parties to file or contest future short supply petitions for spurious reasons. To address this problem, negotiators devised a system that would essentially equate petitions to effective offers to buy and responses to effective offers to supply. This system was aimed at replicating normal business transactions between actual apparel makers and textile producers. However, with more than a year of practical experience, we have seen the process devolve into a mechanism for undermining the basic intent of the commercial availability process through gerrymandered fabric constructions and a superficial due diligence process.

In its submission to CITA, the industry identified several areas of concern and asked CITA to develop a system that sustains the original intent of the CAFTA commercial availability process. Going forward, if the integrity of the short supply process is to be upheld, CITA will need to revise its procedures to ensure that:

1. A company has conducted extensive due diligence including direct meetings with potential suppliers before filing a formal petition;
2. Petitions are submitted and decided upon based on the major characteristics of the product in question;
3. Petitions are based on the component item that may be in short supply as opposed to downstream products; and
4. Petitions based on unenforceable specifications and production techniques are rejected from the outset.

A copy of the letter to CITA outlining our concerns and objectives regarding the CAFTA short supply model is attached.

Tariff Phase-Out Schedules:

With respect to tariff phase-out schedules, the U.S. textile industry has always maintained that these schedules must reflect fair market principles. You are probably asking what does this mean? What this means is that under FTAs, tariffs should be phased out in a manner which ensures U.S. industry is not placed at a competitive disadvantage against manufacturers in the FTA partner country because of government subsidization including no-cost or low interest loans, export tax credits, currency manipulation, and transportation and energy subsidies to name a few.

The textile industry is a capital intensive industry and it takes U.S. manufacturers years to pay down and write off the costs of these investments. When competitors in FTA partner countries do not face

the same cost structures and pressures because of government assistance, then we believe this should be accounted for in the tariff treatment of their products in order to give U.S. manufacturers time to adapt and adjust to the new competitive environment. When government subsidies are prevalent and without such consideration, any benefits intended for the U.S. textile industry will be lost.

Customs Enforcement:

Finally, but most importantly, as the U.S. continues to pursue trade liberalization through free trade agreements, it is vitally important that customs enforcement programs, especially those focused on textiles where fraud is a major challenge, be given priority consideration. As you know, NCTO has worked closely with Congress to ensure adequate funding is provided to the textile division within U.S. Customs and Border Protection. It is equally important that the necessary tools to adequately enforce these agreements be provided for under the provisions of the FTA as well.

Unfortunately, despite increased funding by Congress to Customs and Border Protection for textile enforcement activities and the inclusion of strong customs enforcement provisions in many of our FTAs, the textile enforcement program is in chaos.

Given the implementation of a myriad of new FTAs and expansion of unilateral preference programs, in early 2006 U.S. industry met with Customs to forge a new partnership aimed at rebuilding a strong textile enforcement program capable of meeting the new challenges posed by these programs. As part of this meeting Customs committed to working with industry to build a strong textile enforcement program, that the industry would have regular input and feedback on textile enforcement efforts and that both the industry and Congress would receive quarterly reports on those efforts. True to that commitment, the lines of communication between Customs, industry and Congress were strengthened and information regarding textile enforcement activities was shared regularly. Indeed, as part of this effort, we were pleased to report that Customs made significantly increased seizures of illegal textile imports.

Unfortunately, during the past twelve months, the cooperation and communication framework that we worked so hard to develop has broken down and textile enforcement efforts have become a “black box” for the industry. Much of this problem stems from a Customs decision made approximately one year ago to move the textile enforcement division from Field Operations to a new Office of International Trade. This decision was made without any opportunity for our industry to provide input, despite the fact that we had the most to lose by such a transition. This decision also occurred despite the fact that nearly half of all illegal fraud concerning Customs is textiles related and clearly an enforcement issue as opposed to an international trade policy issue.

Once this transition took effect, we met with the new Customs officials to express our concerns about the transition, particularly regarding its potential impact on seizures and detentions and the textile division’s ability to mount special operations. We recalled the bureaucratic nightmare that a similar move (into a Strategic Trade Division) caused back in the late 1990’s; a move that was eventually reversed.

Unfortunately, shortly after this meeting, Customs halted its quarterly reporting of textile seizure and detention information to the industry and reported to the industry and the Congress that CBP would be cutting back on seizure and detention efforts in favor of auditing, a practice which the industry and many members of Congress have strongly opposed because it has repeatedly been shown to be ineffective in deterring fraud with production-based rules of origin.

We are also concerned that vital special operations which target China transshipments and illegal trade through our free trade and trade preference regions have been curtailed as well. It is concerning that the textile manufacturing sector and the U.S. Congress is having information withheld from it about vital enforcement efforts paid for with U.S. taxpayer dollars and specifically designated by Congress. To put this in context, Customs operates a regular avenue of communication with the importing community through the Commercial Operations Advisory Committee (COAC) but has shut the information door on the domestic industry.

This anti-enforcement approach is occurring during a period of time when the industry is more dependent than ever on proper enforcement of our trade agreements. As trade agreements have proliferated, China and others have sought to illegally ship products through these trade areas at an increasing rate to gain the benefits of duty-free access. And unfortunately, they are being increasingly successful thanks to the lack of effective enforcement measures within CBP. For example:

- Last year, the U.S. Census reported that more combed carded yarn was exported to the CAFTA region in 2005 than was actually produced in the United States. China and others are shipping containers to U.S. ports and then sending them to the CAFTA region and then claiming CAFTA preferences.

- US mills are increasingly reporting losing orders to companies that claim to have facilities in the United States but, upon investigation, those facilities turn out to be non-existent but instead are conduits for Chinese-made textile products.

- Despite very limited resources, we understand that Customs is increasing inspections of companies in trade preference areas with proven compliance records while decreasing inspections of high risk companies. Such practices increase pressure on good players to move their operations to Asia while increasing incentives for bad players to move to trade preference areas.

From our perspective, effective textile enforcement efforts are essential if the U.S. textile industry is to continue its support for a trade liberalizing agenda and also for its very own survival in this competitive climate. At the same time, given the high fraud rates within the textile and apparel sector, this sector should carry a priority for national security reasons as well.

I know this Committee understands that the industry's support for future trade agreements is impossible without faith and confidence that the rules will be effectively enforced; for these reasons, recent actions by Customs management are all the more puzzling because they come at a time when the Administration and Congress are trying to build support for trade policy, but has encountered increasing opposition because U.S. workers and companies no longer believe that these agreements will be enforced. With public concern over imports from China at an all time high, we think it is a terrible mistake for Customs to reduce its enforcement efforts and resources regarding textile enforcement.

Peru, Panama and Colombia Free Trade Agreements

Generally speaking, the Peru, Panama and Colombia Free Trade Agreements are solid agreements that adhere to the general principles outlined earlier -- strong rules of origin with limited exceptions; short supply procedures that are intended to be fair and balanced, tariff phase-out schedules which reflect fair market principles, and strong customs enforcement rules and regulations

On paper, these agreements are VERY GOOD agreements that should provide significant opportunities for the textile and apparel industries in the United States and the FTA partner countries. At the end of the day, however, these agreements are only as good as the rules and regulations written to enforce them, and the day-to-day activities which actually bring these mechanisms to life and give meaning to the FTA concept. If recent history is to serve as a guide, the U.S. textile industry has great justification for concern as to whether these agreements can actually live up to the potential opportunities embodied in the framework of these FTA models. The opportunity is there, but there are now serious concerns about whether the U.S. government is committed to ensuring that this opportunity is actually achieved. At this time, NCTO supports passage of these agreements, but if our members feel that Customs will not effectively enforce these programs, as well as much larger existing agreements, then that support could well be jeopardized.

The reality is that the U.S. textile industry depends on exports for its very survival. As mentioned earlier, the U.S. textile industry is the third largest exporter of textile products in the world exporting more than $16 billion in 2005. Without export markets, especially in the Western Hemisphere, our industry would simply not exist.

As the apparel industry has migrated out of the country and our industry has adapted and worked aggressively to build markets in other parts of the world, primarily the Western Hemisphere where we maintain a competitive advantage in the apparel trade due to speed to market. If the U.S. textile industry is to remain competitive against Asia, especially China, it must have a predictable and stable duty-free trading platform in this hemisphere that is aggressively enforced. The Peru and Colombia FTAs are key components in developing and growing this platform.

For instance, since 2002, U.S. textile exports to Peru have grown from $9.8 million to almost $24 million in 2006. While Peru is still a small market compared to the NAFTA/CAFTA regions, this growth represents an almost 150 percent increase in the value of our exports to Peru in only three short years. With respect to Colombia, in the Andean region, Colombia accounts for 80 percent of U.S. textile exports and U.S. yarn and fabric exports to Colombia have increased by 84 percent since 2002 and now total $167 million.

Unfortunately, both of these countries, and the Andean region as a whole, have recently experienced declines in qualifying apparel imports to the U.S. as well as its share of the U.S. import market. These declines are primarily due to competition from low-cost Asian imports, especially China.

The same holds true for the U.S. textile industry. Since China joined the WTO in 2001, the U.S. textile and apparel industries have lost 365,000 jobs, this represents a 38 percent decrease of our entire workforce. In fact, the industry lost 44,500 from 2005 to 2006 alone. The current environment is unsustainable long term, and not just for us, but for the more than two million textile and apparel workers throughout the U.S./NAFTA/CAFTA/ANDEAN region.

Members of Congress and the Administration continue to emphasize the importance of these agreements from a national security perspective, and we agree that these FTAs have important national security implications. However, if the U.S. government fails to enforce these agreements then the national security concerns will only be exacerbated rather than enhanced by these proposals as hundreds of thousands of workers in Peru and Colombia are left without jobs and are forced to resort to the drug trade or to illegally migrate to the U.S. for work. Under both scenarios, the lack of a comprehensive enforcement policy with respect to these agreements carries grave consequences for the United States.

The potential for increased trade and cooperation among the textile and apparel industries of the U.S. and Peru and Colombia as a result of these FTAs is significant. Our industry is at the mercy of the U.S. government when it comes to reaping these benefits. These agreements can and should work – both for U.S. manufacturers as well as for manufacturers in Peru and Colombia. We implore this Committee to exercise its oversight and due diligence in ensuring that the government lives up to its end of the bargain and that a win-win scenario is created for all parties.

U.S. Korea Free Trade Agreement

As an overall concept, the notion of an FTA with Korea has been problematic for the U.S. textile industry. Since Korea is a large textile-producing country with a vertically integrated industry that has historically enjoyed extensive support from its government, NCTO members have repeatedly stated they do not expect significant new export business to be generated from an FTA. In addition, portions of the U.S. industry are very concerned that an FTA could significantly harm existing U.S. business and trade flows, particularly from the CAFTA, NAFTA and ANDEAN regions.

The Korean Federation of Industries confirmed these suspicions when it concluded that it expects Korean textile exports to increase by 25% or $400 million during the first year of the agreement. The Congressional Research Service cites an ITC study[2] delivered to USTR before the negotiations began which concurred that Korean textile producers, not U.S. producers, are expected to be big winners if this agreement is enacted into law.

As a point of context, the U.S. textile industry has experienced large-scale plant closures and employment declines since the Asian currency crisis in 1998 and the resulting proliferation of undervalued government managed currency regimes throughout Asia, including China and Korea. These sharp declines in Asian currencies, which average around 40 percent, have enabled Asian apparel prices to fall by 34 percent. These artificially low prices have led to the worst crisis in the industry's history. Furthermore, the removal of quotas beginning in 2002 only exacerbated the impact of these mercantilist currency policies.

The U.S. textile industry is concerned that Korea, as a top supplier to the U.S. market in more than 20 sensitive textile and apparel categories, poses a significant threat. These concerns are magnified by the fact that Korea has a proven history of both dumping man-made fiber textile products in the U.S. market (as well as elsewhere) and of transshipping goods from China, a country with which it shares a common border and in which Korean textile firms have made significant investments. Also, the development of large joint industrial zones with North Korea which offers a supply of labor reportedly even cheaper than Vietnam and which specializes in textile production, raise additional concerns for the U.S. industry.

It is in this context that NCTO asked that sensitive textile and apparel products, including but not limited to products under safeguard with China, receive the maximum tariff phase-outs allowed in an agreement with Korea. This request follows historic precedence. Tariff phase-outs in sensitive products under the NAFTA agreement were ten years long and covered 75 percent of textile tariff lines. The phase-out period is particularly important as textile and apparel tariffs are relatively high and therefore the impact of tariff reductions needs to be spread out in as long of a timeframe as possible. Unfortunately, as we will see, USTR chose instead to give Korea immediate duty-access to almost 90 percent of all textile and apparel tariff lines.

[2] "The Proposed South Korea-U.S. Free Trade Agreement (KORUS FTA)", Updated April 23, 2007, Congressional Research Service, p. 30.

In view of South Korea's history as a major transshipment center, NCTO also asked the government to include the strongest customs enforcement language possible as well as sufficient customs resources to effectively enforce the agreement. Other key requests included a yarn forward rule of origin with no loopholes and the inclusion of a regional pocketing requirement. I will now briefly review the textile results of the negotiations.

U.S. - Korea Textile Negotiation Results:

Regarding the industry's key requests, the government was able to include a number of them. These include a yarn forward rule of origin with no loopholes and strong customs enforcement language, which is an essential element in deterring illegal transshipments.

Even with these elements, there remains widespread concern among NCTO member companies that a Korean FTA will, when fully in force, cause significant damage to the U.S. textile industry. U.S. producers are particularly concerned about potentially damaging exports of Korean man-made fiber yarns and fabrics, knit fabric, socks, sweaters, shirts and trousers in addition to transshipments of many sensitive apparel items from China.

This concern has several root causes. These include overexpansion of the Korean textile industry by the Korean government that has resulted in the development of excess manufacturing capacity. As a result, many Korean textile manufacturers now see a duty-free U.S. market as an inviting target for excess supply. This concern is particularly strong in the man-made fiber sector which reports that Korean textile conglomerates frequently resort to predatory pricing in export markets. In addition, the ability of South Korean textile conglomerates or chaebols to use their allies in the banking sector to absorb losses over long periods of time also raises concerns and appears to remain unaffected by this agreement.

In addition, with intense competition in the global textile industry and the prevalence of very low margins, U.S. textile companies believe that the removal of significant U.S. tariffs (some as high as 25 percent) will mean the difference between some U.S. companies staying in business and closing their doors. The fact that South Korea's government practices a mercantilist currency policy that keeps the won at artificially low levels raises additional concerns[3].

Also of strong concern is the likelihood that China, as well as manufacturers in the North Korean Kaesong industrial zones, will use the FTA to transship products duty-free to the United States. Rigorous Customs enforcement lies at the very heart of free trade agreements, particularly in sectors such as textiles where unscrupulous importers can save hundreds of millions of dollars by evading duties.

China's ability to underprice garments made in the CAFTA, NAFTA and Andean regions, which the U.S. textile industry relies upon for the majority of its exports of its yarns and fabrics, has been well demonstrated in the past. In categories where China has had quotas permanently removed, Chinese market has rapidly increased from around 10 percent to around 66 percent. (The next highest supplier is Thailand at 3 percent.) As a result, CAFTA, NAFTA and Andean market share has fallen by half or two thirds. Despite importer claims that they will retain significant business in the CAFTA, NAFTA and Andean region for quick turnaround purposes, the truth is that this business represents only a fraction of the production currently being sourced out of the region.

[3] NCTO notes that while TPA authority requires the U.S. government to take into account currency manipulation in FTA negotiations, KORUS is yet another in a string of FTAs that ignores this issue.

Customs Enforcement:

Industry concerns over whether Customs management has the willingness and determination to properly enforce textile agreements have been growing over the past several years and were outlined extensively earlier in my testimony.

CBP' retreat on textile enforcement is especially troubling in regards to Korea because Korea has been the target of serious Customs inquiries during the recent past and has been a major transshipment point for Chinese products since almost the time when China was first put under quota over twenty years ago. Last year U.S. Customs and Border Protection conducted two Special Operations – Seoul I and Seoul II – targeting Korea. This was the first time the agency conducted two operations within the same year focused on the same country. The agency was so concerned with the high levels of fraud and transshipment found during the first operation that it conducted another operation several months later.

Textiles have the highest fraud rate of any industrial commodity, accounting for 40 percent of all commercial fraud and South Korea has proven to be an epicenter of such activity. For Customs to pull back its commitment to the textile enforcement program on the eve of signing a new FTA with Korea sends an unmistakable signal to the domestic industry that textile enforcement will be minimal if this agreement becomes law.

Again, I cannot emphasize strongly enough how the recent actions by Customs to pull back from a proven and effective enforcement regime have raised serious concerns within the industry, particularly in regards to this agreement. If textile manufacturers do not have confidence that effective enforcement programs will continue to exist in the future then even beneficial FTAs will lack value and importance for the industry.

Tariff Phase-outs Schedules:

Regarding tariff phase-outs, the NCTO member companies were angered to learn that, contrary to past agreements, 87% of textile and apparel tariff lines, covering more than 50% of 2006 trade were given immediate duty phase-outs under the U.S.-Korea FTA. Many sensitive textile and apparel lines were included on this list. This was done despite the fact that USTR knew full well, both from USITC reports and from industry advisors, that Korea posed a real and immediate threat in these product areas.

To understand our dismay, imagine that you are a business and the U.S. government has just enabled one of your biggest competitors to cut prices 18% overnight. This is exactly what will happen under this Agreement if you make socks in this country. Korea shipped $80 million worth of socks to the U.S. last year with duties averaging 18%. On day one of this agreement, those duties go to zero. How are U.S. companies going to adjust to this hit? The answer is they can't, they will simply close their doors and go out of business.

Socks are not the only example. This list includes many sensitive items for which the industry requested the longest possible tariff reductions. These include sweaters, brassieres, swimwear, man-made fiber shirts, certain man-made fiber filament and staple yarns and fabrics (including elastomerics) and carded cotton yarn.

In reviewing the impact of this free trade agreement, it is also important to understand how tariff phase-outs will work. Duties on goods in Basket D are scheduled for a 5-year duty phase-out and

goods in Basket G are scheduled for a 10-year duty phase-out. In fact, these phase-outs will occur, respectively, during the first four and nine years the agreement is in effect. With a five-year phase-out, the first 20 percent duty reduction occurs the day the agreement goes into effect. A year later, the next 20 percent reduction occurs. The net result is a 40 percent reduction in duties during the first 12 months. Further reductions occur in equal installments over the next three years to completely eliminate the duty in a four-year period. The same process applies with the 10-year phase-out: there is a 10 percent duty reduction the day the agreement takes effect, with the next phase occurring 12 months later. Duties are completely eliminated after nine years.

Other points of concern:

While the government did not allow goods from the Kaesong industrial zone to gain access under the U.S.-Korea FTA, the agreement allows for consultations with South Korea on future access. Any such access would require additional legislation but, as the industry has seen occur time and again with "troubled" regions, Congress would likely grant access for North Korean industrial zones once there is a diplomatic breakthrough on the Korean peninsula. As noted earlier, textile production is a major component of the Kaesong project and South Korea projects that over 300,000 workers will be operating in these zones within five years of an FTA passing. Even if these zones were never granted duty-free access, the likelihood of significant transshipments from these zones into the United States remains.

In conclusion, NCTO member companies are worried and concerned about a number of aspects of the Korean FTA and the impact it will have on an industry that is already under enormous pressure in the global marketplace, particularly by countries who refuse to abide by international obligations and pursue trade policies that destabilize global trade in this sector.

Conclusion

In closing, I would like to once again emphasize that the U.S. textile industry is supportive of trade; in fact, our livelihoods now depend on it. But a trade at any cost policy that is more about achieving foreign policy and social objectives than it is about creating an open, transparent and enforceable trade environment means that U.S. manufacturers will continue to lose.

People in America are worried. They are worried about how they will pay their mortgage and send their kids to college. They are worried about their spouses and children who are serving in Iraq, Afghanistan and many other places around the world. These are unsettling times. Despite this fact, many Americans have demonstrated a willingness to sacrifice some of their own economic security in the name of national security and the greater democratic good. I would posit, however, that without economic security, we cannot have national security. Therefore, it is up to Congress to ensure that effective trade policies like those embodied in the Peru and Colombia FTAs are advanced and that the U.S. government fulfills its commitment to U.S. industry through effective enforcement of these agreements.

On the other hand, Congress also should ensure that poorly developed trade frameworks like the one incorporated under the U.S.-Korea FTA is carefully evaluated and, where necessary, renegotiated, before giving it the congressional seal of approval.

But even more importantly, Congress must re-right the trade equation with China so that U.S. workers, not just U.S. consumers, win as well. Congress must pass a strong currency bill that includes the ability of U.S. companies to defend themselves against China's currency manipulation through filing countervailing duty cases.

This House is supposed to be the body of the people, and as such, the people of these United States, especially those who work in the U.S. textile industry, expect their elected officials to look out for what is in their best interest when considering whether or not to lend your support to these agreements. We strongly encourage you to carefully consider the concerns we have outlined in our testimony today when making this difficult decision.

Thank you.

Addendum:

NINE STEPS TO A FAIRER, MORE EQUITABLE TRADE POLICY

1. **Pass Strong Currency Legislation:** The Congress should pass and the President should sign into law meaningful and effective legislation that allows U.S. manufacturers to offset the benefits of the undervalued Yuan. In our opinion, the most effective legislation currently before the U.S. Congress is a bill introduced by Representatives Ryan and Hunter – the Currency Reform for Fair Trade Act or H.R. 2942. This legislation would allow U.S. industry to file countervailing duty cases against China's currency manipulation. This is a reasonable, targeted approach that provides impacted industries with a means of defending themselves without penalizing unaffected parties. Other legislation, such as bills recently passed by the Senate Finance and Banking Committees are too weak because they do not address the subsidy component of currency manipulation and provide numerous escape clauses that would allow the administration to "opt out" even when action is justified.

2. **Extend or Replace the Current China Safeguard**: Congress and the Administration should ensure that the textile safeguards currently in place against China are either extended or replaced until China fulfills all of its WTO-accession commitments. The textile safeguards that have helped to prevent China from monopolizing the U.S. textile and apparel markets in key product categories will expire on January 1, 2009, and they cannot, under WTO law, be renewed.

   In addition, the U.S. government should expand third-country dumping provisions to grant apparel producers in the NAFTA/CAFTA regions the right to bring anti-dumping actions against Chinese apparel exporters who damage their own vital export markets in the United States. Since the passage of NAFTA and CAFTA, textile and apparel sectors in the region have become integrated with the U.S. supplying most of the yarns and fabrics and the NAFTA/CAFTA regions providing the apparel assembly. Ample precedent exists in the WTO for granting apparel producers in the entire region the right to seek redress for dumped goods.

3. **Create a Comprehensive Subsidy Database**: Establish a comprehensive subsidy database on China at the Department of Commerce that can be utilized by government and industry. The U.S. government still refuses to create a database of the subsidies the Chinese government provides to its industry. Instead, the government relies primarily on what China itself has notified as subsidies, a list that is laughably small and incomplete. And even then the Commerce Department's database is not up to date – the government's subsidy review page on the Commerce Department's website has not been updated since 2004[4]. The most noteworthy observation here is that according to the Commerce Department website, China is not listed as employing a single subsidy!

[4] Commerce countervailing duty websites by country and type of subsidy:

4. **Increase Dumping and CVD Assistance to Small and Medium-Sized Manufacturers**: The government should increase assistance to small and medium-sized manufacturers so that they can afford to pursue dumping and countervailing duty (CVD) cases. CVD cases cost several hundred thousand dollars to file and dumping cases typically cost more than one million dollars; costs that are too steep for most small and medium-sized businesses to pay, particularly when those businesses are already losing money because of dumping. The Commerce Department should follow the lead of the European Union by shouldering more of the administrative and financial burden in complying with the complex rules and regulations that the Department imposes.

5. **Increase Enforcement Efforts at USTR and the Department of Commerce:** Today, trade enforcement is seen as a career dead end within the U.S. government; instead, negotiating new agreements rather than enforcing existing agreements is the best way to advance within the ranks. Commerce and USTR need to be restructured to give trade enforcement a higher priority and more status within the agencies. On top of enhanced focus on enforcement, these efforts also need to be greatly expanded. The U.S. government should be conducting ongoing reviews of Chinese government subsidy and support programs and taking action at the WTO and through U.S. trade remedies when warranted.

6. **Review China's Government Support of Its State-Owned Industrial Sectors, Including Textiles, and Penalize Illegal Transactions**: Over the past five years, China's government has forgiven tens of billions of dollars of debt in its state-owned manufacturing sector. This practice has salvaged countless unprofitable enterprises that would not have survived in a free market system. These enterprises, which comprise roughly half of China's textile assets, are notorious for suppressing prices to absurd levels, often below the cost of raw materials. Last year, China announced that it was liquidating almost $600 million in debt to a major Chinese textile manufacturer that it had previously stated had been privatized.[5]

   These state-supported enterprises essentially operate as state employment agencies rather than market-based companies and their pricing practices have caused more damage to legitimate textile producers in the United States and elsewhere than anything else. Because of financial support from the Central Government, textile manufacturers in China can offer whatever price necessary to make the sell and grow its market share, a practice against which no other producer in the world can compete.

   In addition, China continues to effect privatization schemes that appear to transfer huge state-owned industrial enterprises to the private sector at virtually no cost. All of these actions are in direct conflict with China's WTO commitment to treat state-owned enterprises as if they were market entities."

7. **Increase and Reform Customs Enforcement Efforts Targeting China:** Recent newspaper headlines regarding widespread recalls of Chinese food and consumer products are yet another symptom of major enforcement issues involving China – primarily that U.S. Customs has become a trade facilitation, rather than trade enforcement, agency. With respect to textiles, this fact recently became all the more evident when the textile enforcement branch was transferred from the Operations Division into a trade facilitation office. This reorganization occurred despite strong opposition from U.S. industry and in direct conflict to the fact that more than half of all Customs fraud occurs in the textile and apparel sector. CBP needs to intensify its enforcement efforts, particularly in the textile area. As with the Commerce Department and USTR, enforcement has

[5] 12/1/2005: http://www.ncto.org/newsroom/pr200539.asp

now become a dead-end career path within Customs and this is not likely to change without a change in priority.

8. **Develop a More Effective Enforcement System that Holds U.S. Importers and Consignees Responsible for the Products They Import and Provides for Stronger Penalties for Those Who Violate the Law**: U.S. importers and consignees should and must be held responsible for the products they import.

   With respect to the recent spate of product recalls from China, fault does not lie with the Chinese manufacturer; rather, the fault lies with the U.S. company responsible for importing that product to the U.S. market. If the public at large and U.S. policymakers fail to recognize this important point, then any solutions will only be temporary band-aids that address a symptom but the not the underlying disease.

   U.S. laws and regulations can only be applied to entities operating within U.S. borders. U.S. law enforcement and product safety officials do not have the authority to arrest someone in China or to levy fines on a business in China for poor practices. What they do have authority to do is to hold individuals or businesses operating in the U.S. to account when the products they import are found in violation of U.S. laws and regulations. These violations can be safety-related, but in the case of textiles and apparel could also include violations of rules of origin claims.

   With respect to textiles and apparel, rules of origin are the cornerstone of our free trade agreements and preference programs. In the history of the textile program, un-enforced rules have been a proven access point for large-scale fraud that displaces legitimate production both in the U.S. and in the beneficiary country(s) involved. NCTO and our member companies have seen time and again how unscrupulous actors have knowingly violated rules and regulations governing U.S. preference and free trade programs to gain duty-free access to the U.S. market, with China being the worst offender. In fact, the textile and apparel trade has the highest fraud content of any manufactured good. Therefore, it is imperative that the rules and regulations governing this trade are effectively enforced and the only way to do this is through the importer or consignee.

   U.S. regulations governing the importers, however, are weak and often times these importers will appear, disappear and then reappear under new names to avoid penalties and fines and the U.S. government does nothing about it. In considering future FTAs and other trade programs, Congress and the Administration should ensure that these agreements are written in a way that provides for meaningful and effective customs enforcement by requiring the ultimate consignee of the product, i.e. the retailer or the company owning the brand name responsible for rule of origin violations. In the 2005 ITC case U.S. v. The Pan Pacific Textile Group[6], the Court ruled that liability could be extended to the consignee when the consignee has direct input into how the transaction is structured. If the goal is to ensure that safety standards and rules of origin are adhered to then the law should be broadened to ensure that the consignee is also responsible for the products its sells or that bears its brand name.

9. **Develop a System for Penalizing Companies Importing Products Which Were Made by Companies Who Pollute the Environment:** A recent front page Wall Street Journal expose on the Chinese textile industry revealed that continuing demands by U.S. importers for lower prices are playing a key role in the environmental catastrophe that is now unfolding across China. The Journal notes that "one way China's factories have historically kept costs down is by dumping waste water directly into rivers."

[6] United States Court of International Trade. U.S. v. Pan Pacific Textile Group. Slip Op. 05-107. Court No. 01-0122